

Audit

Report



OFFICE OF THE INSPECTOR GENERAL

CONTROLS OVER FUEL PAYMENTS

Report Number 91-111

July 16, 1991

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Department of Defense

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The following acronyms are used in this report:

DFAMS.....	Defense Fuels Automated Management System
DFAS.....	Defense Finance and Accounting Service
DFR.....	Defense Fuel Region
DFSC.....	Defense Fuel Supply Center
DLA.....	Defense Logistics Agency
GAO.....	General Accounting Office

July 16, 1991

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on the Controls Over Fuel Payments
(Report No. 91-111)

We are providing this final report for your review and comments. We evaluated collection procedures for overpayments to contractors, write-off procedures for uncollected overpayments, and controls over fuel payments at the Defense Fuel Supply Center (DFSC). The audit showed that DFSC was not collecting overpayments made to bulk fuel contractors in a timely manner. Overpayments remained outstanding for extended periods, which could cause the U.S. Treasury to incur about \$2.1 million of unnecessary interest costs over a 6-year period. DFSC had not met the intent of the recommendation in General Accounting Office Report Number AFMD-87-30, dated May 13, 1987, that negative accounts payable balances be classified as accounts receivables and promptly collected. Also, DFSC improperly wrote off about \$553,000 of debts owed to DFSC by contractors. Additionally, some Defense Fuel Regions (DFR's) did not ensure that material inspection and receiving reports for fuel deliveries were obtained and properly certified before reporting delivery information to DFSC for support of payments to contractors.

On March 7, 1991, a draft of this report was provided to the Director, Defense Logistics Agency. Comments on the draft report were received from the Comptroller, DLA, on May 10, 1991, and were considered in preparing the final report. Recommendations A.1. and C. remain unresolved. The monetary benefits associated with Recommendation A.2. are also unresolved. We request that further comments be provided on Recommendation A.1. to clarify that DFSC will no longer establish negative accounts payable balances in its accounting records before accounts receivable balances are established. We also request further comments on the \$2.1 million in monetary benefits identified for Recommendation A.2. because the Comptroller, DLA, did not agree that all the monetary benefits would be achieved. The Comptroller, DLA, nonconcurred with Recommendation C. stating that the recommendation would generate more work and not improve internal controls. He indicated that receiving activities can directly input receipt data without going through the DFR's. The text of Finding C. has been revised to focus on the procedures and practices used by DFSC and the DFR's to support payments to contractors. However, our position remains that DFSC needs to ensure that properly certified material inspection and receiving reports are obtained by DFR's before submitting receipt data into

the Defense Fuels Automated Management System. We, therefore, request that DLA reconsider its nonconcurrence with Recommendation C. DoD Directive 7650.3 requires that all audit recommendations be resolved promptly. Therefore, we request that the Director, Defense Logistics Agency, provide comments on Recommendations A.1. and C. and the monetary benefits associated with Recommendation A.2. by September 15, 1991.

If you nonconcur with the estimated monetary benefits or any part thereof, you must state the amount you nonconcur with and the basis for your nonconcurrence. Recommendations and potential monetary benefits are subject to resolution in accordance with DoD Directive 7650.3 in the event of nonconcurrence or failure to comment.

The courtesies extended to the audit staff are appreciated. If you have any questions on this audit, please contact Mr. John Gebka at (703) 614-6206 (DSN 224-6206) or Mr. Darrell Eminhizer at (703) 614-6220 (DSN 224-6220). The planned distribution of this report is listed in Appendix G.

E. Jones
Edward R. Jones
Deputy Assistant Inspector General
for Auditing

cc:

Department of Defense Comptroller
Assistant Secretary of Defense (Production and Logistics)

Office of the Inspector General, DoD

AUDIT REPORT NO. 91-111
(Project No. OLC-0026)

July 16, 1991

CONTROLS OVER FUEL PAYMENTS

EXECUTIVE SUMMARY

Introduction. The Defense Fuel Supply Center (DFSC) purchases about \$3.3 billion in bulk petroleum fuel annually. Bulk fuel contracts include an economic price adjustment clause. The contracts provide that the price paid for fuel will be the market price at the time fuel is delivered. The applicable market price is not determined until several months after the delivery date and usually requires that the interim payment to the contractor be adjusted. When fuel prices are rising, underpayments result. When prices are falling, overpayments occur.

Objectives. The objective of the audit was to determine if DFSC control procedures ensured prompt identification and collection of overpayments on bulk fuel purchases. We also followed up on the recommendation contained in the General Accounting Office (GAO) Report No. AFMD-87-30, "Internal Controls Defense Fuel Supply Center's Recording and Reporting Accounts Payable," May 1987, that DFSC classify negative accounts payable amounts as accounts receivable and ensure their prompt collection.

Audit Results. DFSC controls over the recording and collection of overpayments on bulk fuel purchases were inadequate. In addition, controls over the certification of fuel delivery prior to payment were inadequate.

o DFSC did not comply with provisions of the "DoD Accounting Manual," DoD 7720.9-M or the Debt Collection Act when recording and collecting overpayments made to contractors on bulk fuel purchases. In addition, DFSC did not meet the intent of the GAO recommendation to classify and record overpayments to contractors as accounts receivable instead of negative accounts payable. If overpayments continue to remain outstanding for extended periods before being collected, the U.S. Government could incur unnecessary interest cost of \$2.1 million during the next 6 years (Finding A).

o DFSC was writing off debts owed by contractors without taking appropriate collection actions. As a result, we identified six debts, valued at about \$553,000, that were improperly written off (Finding B).

o DFSC paid contractors for fuel, valued at \$29.9 million, without adequate evidence that fuel was delivered. Making payments to contractors without assurance that fuel was received was a weakness in DFSC's internal control over the fuel payment process (Finding C).

Internal Controls. Internal controls were insufficient to ensure that contractors were promptly billed for overpayments and assessed interest for late payments, write-offs were valid, and fuel deliveries were properly certified before contractors were paid. See Findings A, B, and C for details on these weaknesses and page 2 for our review of internal controls.

Potential Benefits of Audit. We identified potential monetary benefits totaling about \$2.7 million. Other potential benefits include improved liquidity of the Defense Stock Fund and U.S. Treasury and strengthened internal controls (see Appendix E).

Summary of Recommendations. We recommended recording overpayments as accounts receivable, prompt submission of billings and assessment of interest for debts contractors owed DFSC, compliance with write-off procedures, and proper verification of material inspection and receiving reports.

Management Comments. Comments from the Defense Logistics Agency were received on May 10, 1991. DLA concurred with four of five recommendations. Although DLA concurred with Recommendation A.1., we have requested that DLA clarify the actions taken to ensure that DFSC discontinues using negative accounts payable balances instead of accounts receivable balances for debts owed by contractors. The discussion for Finding B. and Recommendations B.1. and B.2. were revised to provide that uncollected debts be forwarded to the Defense Finance and Accounting Service rather than Headquarters, DLA, to reflect recent Comptroller, DoD guidance. We have also requested that DLA reconsider its nonconcurrence with Recommendation C. on the need to have the Defense Fuel Regions verify that fuel was received before DFSC pays the contractors. Because DLA disagreed with the projected \$2.1 million in monetary benefits associated with Recommendation A.2., but had concurred with the recommendation that will result in the monetary benefits being achieved, we requested DLA to further comment on the \$2.1 million in monetary benefits. DLA's responses are further discussed in Part II of the report. The full text of DLA's responses is included in Part IV of the report.

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This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Information Officer, Audit Planning and Technical Support Directorate at (703) 693-0340 (DSN 223-0340).

PART I - INTRODUCTION

Background

Bulk fuel purchases. The Defense Fuel Supply Center (DFSC), a component of the Defense Logistics Agency (DLA), located at Cameron Station, Alexandria, Virginia, is responsible for bulk fuel purchases. DFSC has 10 regional offices that verify fuel deliveries, and monitor storage and distribution at 213 Defense fuel supply points, worldwide. DFSC's Accounting and Finance Division is responsible for maintaining financial records and processing payments, collections, write offs, and offset actions for bulk fuel transactions. Before August 9, 1988, these accounting and financial functions were performed by DLA's Administrative Support Center.

DFSC purchases about \$3.3 billion in bulk fuel, annually. Fuel contracts include an economic price adjustment clause. The contractor is paid an interim price at the time that fuel is delivered. The interim price is determined based on the most recent available pricing data from the Department of Energy. A final price is determined several months after the delivery of fuel when the Department of Energy pricing data is published for the time period when the delivery was made. The final price could be higher or lower than the price used on the contractor's interim invoice. A rise in fuel price results in an underpayment to the contractor, and a fall in price results in an overpayment.

Objectives

The audit objective was to determine if DFSC had sufficient internal controls to ensure prompt identification and collection of overpayments to contractors on bulk fuel purchases. We also followed up on the recommendation made in General Accounting Office (GAO) Report Number AFMD-87-30, "Internal Controls Defense Fuel Supply Center's Recording and Reporting of Accounts Payable," May 1987, that negative accounts payable amounts be classified as accounts receivable and promptly collected.

Scope

Fuel payments. The audit evaluated DFSC's practices for recording and collecting overpayments made to contractors on bulk fuel purchases made by DFSC during FY 1988 and FY 1989, write-off procedures, and controls over fuel delivery documentation and verification prior to contractor payment. We randomly selected a statistical sample of 375 payment vouchers, valued at \$629.6 million, that were paid during FY 1988 and FY 1989. The sample payment vouchers were stratified into three dollar ranges; under \$100,000, from \$100,000 to \$1 million, and over \$1 million. Further details of the sampling plan are discussed in Appendix A.

Audit locations, records, and standards. The audit was made at Headquarters, DLA; Headquarters, DFSC; and five Defense Fuel Regions (DFR's) (DFR-Central, DFR-Northeast, DFR-Pacific DFR-South, and DFR-West). We evaluated DFSC practices to determine if DFSC was in compliance with Public Law 97-365, "Debt Collection Act"; Public Law 97-177, "Prompt Payment Act"; DoD Directive 4140.25; DoD Accounting Manual 7720-9.M; DLA Manual 7000.1; and DFSC operation manuals pertaining to the bulk fuel payment process. Our review included an analysis of basic contracts, contract modifications, payment vouchers, contractor invoices, journal vouchers, debt collection schedules, claims receivable reports, and material inspection and receiving reports.

This economy and efficiency audit was made from November 1989 to October 1990, in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly, included such tests of internal controls as were considered necessary. A list of activities visited or contacted during the audit is shown in Appendix F.

Internal Controls

Controls assessed. We evaluated internal controls associated with the bulk fuel payment and collection process, write offs of contractor debts by DFSC, and processing material inspection and receiving reports.

Internal control weaknesses. The audit identified internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Internal controls were insufficient to ensure that overpayments were promptly billed and collected, write-offs were valid, and fuel deliveries were properly certified before contractors were paid. These internal control deficiencies are discussed in detail in Part II of this draft report. Recommendations in Findings A, B, and C, if implemented, will correct these weaknesses. Monetary benefits will be achieved by collecting \$553,000 from contractors for debts that were improperly written off and by avoiding U.S. Treasury interest costs of \$2.1 million on overpayments retained by contractors for extended periods. Other benefits include improved liquidity of the Defense Stock Fund and interest income for the U.S. Treasury on delinquent contractor payments.

Prior Audits and Other Reviews

GAO Report No. AFMD-87-30 (OSD Case No. 7327), "Internal Controls Defense Fuel Supply Center's Recording and Reporting of Accounts Payable," May 13, 1987, identified weaknesses in the bulk fuel accounting system. GAO found that bulk fuel overpayments were

incorrectly classified and reported, and that debt collection efforts were inadequate. GAO recommended that DFSC classify and report negative accounts payable amounts as accounts receivable as they occur and ensure the prompt collection of the receivables. DLA partially concurred with the need to improve controls over accounts payable data recording and processing. Our review of DFSC's use of negative accounts payable is discussed in Finding A.

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PART II - FINDINGS AND RECOMMENDATIONS

A. OVERPAYMENTS TO CONTRACTORS

DFSC was not complying with the provisions of DoD Accounting Manual 7720.9-M or Public Law 97-365, "Debt Collection Act," or the intent of GAO's recommendation to properly record and promptly collect overpayments made to contractors on bulk fuel purchases. Overpayments made to contractors were classified as negative accounts payable instead of accounts receivable in the accounting records, and DFSC rarely submitted billings to contractors for overpayments. Collections were accomplished by offsetting negative accounts payable balances against later invoices submitted by contractors. When offsets were not made within 30 days, no interest could be assessed against the contractors, as prescribed by the Debt Collection Act, because DFSC had not billed the contractors for the debts. In FY's 1988 and 1989, we estimate that the U.S. Government incurred about \$707,130 in unnecessary interest cost because DFSC allowed contractors to retain overpayments of about \$41.8 million longer than 30 days. If the current accounting and collection practices continue and the same pattern of interest rates and fuel price fluctuations occurs, we estimate that the U.S. Government could incur unnecessary interest cost of about \$2.1 million over the 6-year Future Years Defense Program.

DISCUSSION OF DETAILS

Background

Accounting and collection policy. The Debt Collection Act, as implemented by the DoD Accounting Manual (the Manual), requires DoD agencies to charge interest on debts owed the Government if debts are not paid within 30 days of written notification. DFSC had limited incentives to charge interest to contractors for overpayments because interest assessed against contractors could not be retained by DFSC, but had to be forwarded to the U.S. Treasury. Under the Prompt Payment Act, DoD agencies are required to pay contractors interest if payments are not made within 30 days after contractor billings are received for goods and services delivered. Therefore, DFSC had an incentive to make prompt payments because DFSC had to pay any interest owed to the contractors from its own funds.

The Manual requires that receivables be recorded accurately and promptly to provide timely and reliable financial status on all debts owed the Government. The Manual states, ". . . accounting records for receivables shall be maintained so that all transactions affecting the receivables for each reporting period are included. All debts and accounts that result from the occurrence of any event for which a determination is made that

money is owed to the Government shall be considered as receivables and recorded in the DoD Components' accounting systems at the earliest opportunity."

Accounting practices. DFSC's practices for processing fuel payments emphasized compliance with the Prompt Payment Act, but placed little emphasis on compliance with the Debt Collection Act. Because bulk fuel contracts included an economic price adjustment clause, the contractor was paid an interim price until the final price was determined, which usually resulted in an underpayment or overpayment to the contractor. DFSC recorded and classified underpayments as accounts payable and paid contractors within 30 days. When overpayments were made to contractors, DFSC classified and recorded them as "negative accounts payable." Overpayments were usually collected by offsetting them against later invoices even if invoices were submitted more than 30 days after the overpayment. DFSC rarely billed or collected interest on overpayments made to contractors.

Collection of Negative Accounts Payable

DFSC's negative accounts payable involved millions of dollars in overpayments, yet DFSC was not billing contractors for the overpayments on open contracts although it often took more than 30 days to make an offset against a later contractor invoice. Based on our review of a sample of 375 payment vouchers valued at \$629.6 million from a universe of 8,299 vouchers valued at \$6.6 billion, we projected that 1,493 vouchers (18 percent) had overpayments totaling \$41.8 million that were not collected within 30 days (Appendix A). The specific sample cases with overpayments outstanding from 31 to 245 days (the median was 59 days) are listed in Appendix B.

DFSC did not charge interest on the overpayments that were outstanding over 30 days. (In effect, the contractors had an interest-free loan for the amount of the overpayment.) We projected that a total of \$707,130 in interest was "lost" in FY's 1988 and 1989 on \$41.8 million in overpayments that were not offset or collected within 30 days. We used the effective date of the final price modification to compute interest. If an offset was not taken within 30 days, then we computed the interest that should have been collected from contractors.

In accordance with the Debt Collection Act, the contractors are not required to pay interest unless they are billed for the overpayments. Then, the contractors have a 30-day period to make payment before interest is charged. Concurrently, in simplistic terms, the U.S. Treasury borrows funds to pay the Government's operating expenses, including DFSC fuel purchases. If overpayments are made, the overpayment represents funds the U.S. Treasury had to borrow. Accordingly, the Debt Collection Act requires that interest on overpayments be paid to the U.S.

Treasury. Since the overpayments were not billed and interest not collected, the U.S. Treasury incurred an unnecessary interest expense of \$707,130. In actual practice, the amount of interest collected would be less because most contractors would pay within 30 days of being billed. The Government would then have use of the principal amount sooner, rather than receiving interest. However, if DFSC continues with its current accounting and collection practices and the same pattern of interest rates and fuel price fluctuations occurs, we estimate that the U.S. Treasury could incur unnecessary interest cost of about \$2.1 million (\$707,130 multiplied by 3) over the 6-year Future Years Defense Program.

The \$2.1 million in estimated interest costs is a reasonable amount based on the market conditions for both fuel prices and interest rates. Fuel prices fluctuate over time. For the audit period selected (FY's 1988 and 1989), DFSC paid from a low of \$.49 a gallon to a high of \$.66 a gallon for jet fuel. During this time period, two significant swings in fuel prices occurred. The prices paid enabled us to effectively evaluate payments to contractors by examining DFSC's payment practices when prices were rising and declining. The U.S. Treasury rates used by DFSC, for debts owed by contractors, ranged from a low of 8.5 percent to a high of 9.75 percent from FY 1988 through FY 1990. These rates reflect the relative stability of U.S. Treasury interest rates and are considered a valid basis to project future interest costs.

GAO Audit Followup

DFSC did not implement the intent of the recommendation in GAO Report Number AFMD-87-30, dated May 13, 1987, that DFSC classify and report negative accounts payable amounts as accounts receivable as they occur and ensure the prompt collection of those receivables. DFSC did revise its accounting practices in an attempt to comply with the GAO recommendation, but we consider this action insufficient. Before month-end financial reports were prepared, DFSC initiated a journal entry to show the cumulative negative accounts payable balances as accounts receivable. After the month-end financial reports were prepared, another journal voucher reversed the balance from accounts receivable back into negative accounts payable accounts. This procedure caused erroneous financial reports because the accounts receivable balance was never billed to the contractors.

In summary, DFSC continued to classify and record all bulk fuel overpayments to contractors as negative accounts payable and not accounts receivable, as required by the Manual. Also, DFSC did not follow DoD accounting policy that requires agencies to bill contractors promptly, and charge interest as applicable on delinquent accounts.

RECOMMENDATIONS FOR CORRECTIVE ACTIONS

We recommend that the Commander, Defense Fuel Supply Center:

1. Promptly record all overpayments made to contractors as accounts receivable in official accounting records to comply with provisions of DoD Accounting Manual 7220.9-M and bill contractors for overpayments when immediate offsets cannot be made.
2. Assess interest on overpayments retained by contractors in excess of 30 days after being billed to comply with provisions of the Debt Collection Act.

MANAGEMENT COMMENTS

The Comptroller, Defense Logistics Agency, concurred with Recommendation A.1. and stated that DFSC had implemented the following corrective measures.

- o Accounts payable balances are reviewed daily for accuracy and specifically to identify negative entries.
- o Negative entries to accounts payable balances are researched to determine the cause. Using a "worst case" scenario, it takes 30 days to adequately research a negative entry to accounts payable. If the negative entry is the result of an overpayment, the amount is recorded as an accounts receivable.
- o In compliance with the DoD Accounting Manual 7220.9-M and the Debt Collection Act, the "overpayment" is remedied by offsetting the amount owed against a vendor's subsequent invoice. If a subsequent invoice is not "in house" when the overpayment is discovered, a demand letter is sent to the vendor without delay. If the payment is not received in accordance with the demand letter, interest is assessed.

The Comptroller stated that because of the actions taken by DFSC and the procedures being used by DFSC since the audit, no further action is necessary at this time.

The Comptroller, Defense Logistics Agency, concurred with Recommendation A.2. The Comptroller stated that corrective measures have been fully implemented so that DFSC assesses interest on unpaid balances not received within 30 days in accordance with the demand letter.

The Comptroller agreed that the auditors' estimate of \$707,130 for monetary benefits for Recommendation A.2. was reasonable for FY 1988 and FY 1989. However, the Comptroller did not agree that

the projected \$2.1 million in savings over the 6-year Future Years Defense Program was a viable projection because DFSC has changed its accounting and collection practices since the review period of the audit.

AUDIT RESPONSE

Although the Comptroller, Defense Logistics Agency, indicated concurrence with Recommendation A.1., we find that the corrective measures cited are unclear concerning DFSC's use of negative accounts payable balances. The Comptroller's comments indicated that DFSC will continue to record negative accounts payable balances instead of immediately establishing accounts receivable balances when overpayments to contractors occur. After the negative accounts payable balances are established, DFSC does research to determine if the balances can be offset against current contractor billings. We have obtained copies of DFSC monthly journal vouchers as recent as May 1991 that show DFSC continuing to maintain negative accounts payable balances. Additional data indicates that as of March 31, 1991, negative accounts payable balances were \$73.8 million, including \$2.4 million that was over 360 days old. DoD Accounting Manual 7220.9-M does not provide for the establishment of negative accounts payable balances. To comply with the Manual, only a single entry to establish accounts receivable balances is required. We, therefore, request the Director, DLA, to reconsider DLA's position on Recommendation A.1. and clearly state that negative accounts payable balances will no longer be entered into DFSC's accounting records before accounts receivable balances are established.

The comments provided by the Comptroller, DLA, stating that DFSC will assess interest on debts owed by contractors is responsive to Recommendation A.2.

The Comptroller's position on the monetary benefits of \$2.1 million is inappropriate. The Treasury will be able to avoid about \$2.1 million in interest cost during the 6-year Future Years Defense Program specifically because of DFSC's changes in accounting and collection practices in response to our recommendations. The Treasury will no longer have to borrow funds and pay interest costs when DFSC promptly collects overpayments made to contractors. We, therefore, request that the Director, DLA, further comment on the \$2.1 million in monetary benefits related to Recommendation A.2.

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B. WRITE-OFFS OF DEBTS OWED DFSC

DFSC was not complying with provisions of DLA Manual 7000.1, "Accounting and Finance Manual," for writing off debts that contractors owed to DFSC. This occurred because DFSC's Accounting and Finance Office removed negative accounts payable balances (amounts owed to DFSC by contractors) from its financial records without attempting to recover these funds. The removal of negative accounts payable balances above \$600 represented a write-off of debt, which DFSC was not authorized to do without approval from higher authority. As a result, DFSC did not recover \$553,000 from contractors, which reduced the financial resources of the Defense Stock Fund.

DISCUSSION OF DETAILS

Background

Write-off policy. DLA Manual 7000.1, states that the Accounting and Finance Division is primarily responsible for the transfer of all debts of \$600 and more to the Comptroller at DLA Headquarters for further collection proceedings. The Manual also states that DFSC has the authority to write off debts of no more than \$600 per contract; DLA Headquarters can write off debts up to \$20,000 and the Department of Justice can take legal action on debts in excess of \$20,000. DLA was in the process of revising DLA Manual 7000.1 to reflect February 1, 1991 guidance from the Comptroller, DoD, which delegates authority to Defense Finance and Accounting Service (DFAS) to collect debts owed by contractors that are referred by Defense agencies and Military Departments for collection.

Before DFSC can write off a debt, it is required to attempt to recover the amount owed by the contractor. DLA Manual 7000.1 requires that when a debt is recognized, a demand letter will be sent to the contractor requesting settlement of the debt. If the contractor does not respond within 30 days, a second demand letter will be sent requesting settlement from the contractor within 15 days from the date of the second demand letter.

Under DLA Manual 7000.1, DFSC is required to create a contract debt file for amounts above \$600 after all efforts have been exhausted to recover the debt. Under a DFAS Order, dated February 4, 1991, debts must be forwarded to the Debt Collection Branch of the DFAS, Washington Center, or other appropriate center for further action. The Directors of the DFAS centers are authorized to compromise, suspend, or end collection actions on claims that do not exceed \$100,000. Claims exceeding \$100,000 must be forwarded to the Department of Justice for collection actions.

Write-off Practices

Controls were not established to ensure that DFSC's write-off practices were in compliance with policy contained in DLA Manual 7000.1. Under DFSC's procedures, the Finance Branch within the Accounting and Finance Division at DFSC, maintains all negative accounts payable balances that are over 30 days old. The Finance Branch removes these balances from the negative accounts payable register after the first demand letter has been sent to the contractor and no payment is received. The Finance Branch records the removal of negative accounts payable balances by preparing a journal voucher for the write off of amounts owed to DFSC. A copy of the journal voucher is provided to the Stock Fund Section within the Accounting Branch, which is supposed to establish the negative accounts payable as a claims receivable.

Due to inadequate controls, DFSC was writing off negative accounts payable balances owed by contractors without establishing these amounts as claims receivable. We reviewed negative accounts payable registers, claims receivable reports, and debt collection schedules to determine if write-offs of negative accounts payable balances had been established as claims receivable. Records for the write-off of negative accounts payable were incomplete during the period of October 1, 1987, through September 30, 1989. Supporting evidence, such as copies of demand letters, was not being retained to justify the write-off of debts owed to DFSC.

We did, however, identify six contractors' debts, totaling \$552,738, that the Finance Branch improperly removed from the negative accounts payable register (see Appendix C). These six debts were identified from journal vouchers for the write-off of negative accounts payable found in the Finance Branch and were researched through the Accounting Branch. We found that these debts had never been established as claims receivable in the Accounting Branch. Further, DFSC exceeded the \$20,000 limitation established in the Manual for which the Department of Justice was to write off debts. In addition, all of these debts were removed from DFSC's accounting records without approval from DLA Headquarters.

RECOMMENDATIONS FOR CORRECTIVE ACTION

We recommend that the Commander, Defense Fuel Supply Center:

1. Establish controls to ensure that write-off procedures are in compliance with Defense Logistics Agency Manual 7000.1, that demand letters be sent to contractors for debts owed to DFSC, and that if debts are not promptly collected, they are forwarded to Defense Finance and Accounting Service for collection.

2. Establish claims receivable accounts for the six debts owed by contractors totaling \$552,738, submit demand letters for these debts, and if not promptly collected, refer the debts to Defense Finance and Accounting Service for further collection actions.

MANAGEMENT COMMENTS

The Comptroller, Defense Logistics Agency, concurred with Recommendation B.1. and stated that DFSC had implemented corrective measures to ensure compliance with Defense Logistics Agency Manual 7000.1 to preclude the improper write-off of debts owed by contractors. The Comptroller also concurred with Recommendation B.2. to establish claims receivable accounts for debts totaling \$552,738 owed by contractors. DFSC will process the claims for collection in accordance with DLA Manual 7000.1, except that any uncollected debts will be referred to the Defense Finance and Accounting Service. DFSC plans to have action completed on this recommendation by September 1991.

AUDIT RESPONSE

The actions taken by DFSC are responsive to Recommendations B.1. and B.2. We revised Recommendations B.1. and B.2. to require that delinquent contractor debts be forwarded to the Defense Finance and Accounting Service rather than to Headquarters, Defense Logistics Agency. This change was made to reflect a Department of Defense Comptroller memorandum, dated February 1, 1991, that delegated authority to the Defense Finance and Accounting Service to collect debts owed by contractors that are referred by Defense agencies and Military Departments for collection. No further comments are required to Recommendations B.1. or B.2.

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C. BULK FUEL PAYMENT PROCESS

Headquarters, DFSC, paid contractors for bulk fuel, valued at \$29.9 million, without adequate evidence that the fuel was delivered. Payments were made without obtaining properly certified material inspection and receiving reports (DD Form 250/250-1). Making payments to contractors without assurance from a Government representative that fuel was received was a weakness in DFSC's internal control over the fuel payment process.

DISCUSSION OF DETAILS

Background

Authorization for payment. DoD Manual 4140.25, "Management of Bulk Petroleum Products, Storage, and Distribution Facilities," provides that material inspection and receiving reports are to be used to document shipments and receipts of bulk fuel, and that the Government representatives are responsible for dating and signing the completed master copies of the material inspection and receiving reports to certify inspection and acceptance of fuel. The material inspection and receiving report is the document used to support bulk fuel payments. The documentation review process was performed by DFSC's Finance and Accounting Division.

Material inspection and receiving reports were sent to DFSC for review before payments were made to contractors. Headquarters, DFSC, received the material inspection and receiving reports through distribution from either the contractor or Government representatives. DFSC's accounts payable section reviewed the material inspection and receiving reports for proper certification and determined if the quantity and dollar amounts on the reports agreed with the quantity and dollar amount on contractor invoices. In an effort to expedite payments for fuel and to test the Defense Fuels Automated Management System (DFAMS), DFSC also used fuel receipt data in FY's 1988 and 1989 provided by the DFR's and the Military Departments. The DFAMS receipt data (commonly referred to as the P20/P30 report) were used to support payments made to contractors when properly certified material inspection and receiving reports were unavailable.

On December 1, 1989, DFSC implemented new guidance, which stated that the Finance and Accounting Division could rely completely on receipt data generated by DFAMS to support bulk fuel payments to contractors. Upon receipt of the material inspection and receiving report, the DFR's were to input the date of delivery, type fuel, and quantity information into DFAMS, which generated

the P20/P30 Report. For origin and destination deliveries to Air Force receiving activities, the Air Force activities also input data into DFAMS.

Support for Payments

DFSC did not have adequate documentation to support all fuel payments made to contractors during FY's 1988 and 1989. At the DFSC Finance and Accounting Division, we reviewed documentation in support of 375 payment vouchers, valued at \$629.6 million. We examined 623 fuel deliveries for about 869 million gallons of fuel with an estimated value of \$501.3 million made to five of the eight DFR's in FY's 1988 and 1989. We identified 301 deliveries, valued at \$323.7 million, that were not properly supported at Headquarters, DFSC. Copies of the material inspection and receiving reports at DFSC Finance and Accounting Division either were missing or did not contain signatures of Government representatives certifying receipt of the fuel deliveries. The Finance and Accounting Division was required to have certified reports before payments were made to contractors. Since DFSC was also relying on DFAMS data, we visited the five DFR's to evaluate the 301 deliveries without proper support.

At the five DFR's, we found documentation to support 142 deliveries, valued at \$289.4 million, of the 301 deliveries. Of the remaining 159 deliveries without proper documentation, DFSC Headquarters relied on DFAMS data submitted by Air Force receiving activities for 79 deliveries, valued at \$4.4 million. We did not further analyze these deliveries in the scope of this audit since they involved Air Force receiving activities.

For the remaining 80 deliveries, valued at \$29.9 million, four of the five DFR's did not have proper support for the payments to contractors. However, DFSC did not provide the DFR's with guidance that required the DFR's to ensure that the material inspection and receiving report was properly certified before entering receipt data into DFAMS. DFR-Northeast had properly signed material inspection and receiving reports for all deliveries reviewed. DFR-South had one document missing from its fuel records, but all other fuel receipt documents contained the appropriate certification signatures of Government representatives. DFR-Central had 65 fuel receipt documents for \$585,000 that did not have the appropriate certification signatures. DFR-Pacific had six fuel receipt documents missing for \$13.6 million and another five documents for \$3.7 million without a certification signature of a Government representative. DFR-West had three fuel receipt documents for \$12 million missing (see Appendix D).

Prior to December 1, 1989, the DFSC Finance and Accounting Division had the responsibility for reviewing material inspection and receiving reports to support payments to contractors for fuel. When DFSC began relying on data reported in the DFAMS, DFSC did not issue policy guidance to the DFR's requiring that reports be obtained and properly certified before the DFR's entered data on fuel deliveries into DFAMS. Therefore, the DFR's that we visited were unaware that it was their responsibility to ensure that properly certified material inspection and receiving reports were obtained to support payments to contractors for fuel. DFSC policy guidance and management controls at the DFR's are needed to minimize the potential risk of payments being made to contractors for undelivered fuel.

RECOMMENDATION FOR CORRECTIVE ACTION

We recommend that the Commander, Defense Fuel Supply Center, issue policy to require that Defense Fuel Regions ensure that they have accurate, complete, and properly certified material inspection and receiving reports (DD Form 250/250-1) before the DFR's enter fuel delivery information into the Defense Fuels Automated Management System.

MANAGEMENT COMMENTS

The Comptroller, Defense Logistics Agency, nonconcurred with Recommendation C., and stated that the recommendation would require the customer or receiver of fuel to forward a copy of the receipt document to either the DFR or Headquarters, DFSC, and that DFSC would pay the contractor only upon receipt of a certified material inspection and receiving report. The Comptroller stated that this procedure would generate additional paperwork, duplicate the DFAMS process, and slow the payment process. The Comptroller also stated that issuance of such policy would not improve internal controls and explained the procedures to be used by receiving activities that directly input data into DFAMS. The Comptroller noted that customers who receive fuel directly from contractors under destination contracts can directly input receipt data into DFAMS without going through the DFR's.

AUDIT RESPONSE

The Comptroller misinterpreted Recommendation C. The intent of the recommendation was to ensure that controls existed to validate the receipt of fuel before DFSC paid contractors. The recommendation was not intended to require Headquarters, DFSC, to receive copies of every material inspection and receiving report. However, because DFSC now relies on DFAMS data to support payments to contractors, DFSC needs to ensure that DFR's

and receiving activities inputting receipt data into DFAMS are validating the data before entering them. The recommendation would not require any additional paperwork by the DFR or receiver of fuel. Air Force activities receiving fuel delivered under destination contracts would continue to enter properly certified fuel receipt data into DFAMS to support payments to contractors. However, the DFR's would be required to obtain properly certified receiving reports before entering receipt data into DFAMS for all origin contracts, and for destination contracts for the other Military Departments that do not have direct access to DFAMS. The text of Finding C. has been revised to focus on the procedures and practices used by DFSC and the DFR's to support payments to contractors. Appendix D has been adjusted to show only delivery data that the DFR's are responsible for inputting into DFAMS.

To reduce the risk of paying contractors for undelivered fuel, DFSC needs to issue policy guidance that requires the DFR's to ensure that material inspection and receiving reports are certified before receipt data are entered into DFAMS. Relying on DFAMS data without ensuring that the data are supported by certified material inspection and receiving reports, increases DFSC's vulnerability to making payments to contractors for fuel that was not received. We, therefore, request that the Director, DLA, reconsider DLA's nonconcurrence with Recommendation C.

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PART III - ADDITIONAL INFORMATION

APPENDIX A - Sampling Procedure

APPENDIX B - Sample Overpayments With Interest Lost
(FY 1988 and FY 1989)

APPENDIX C - Write-Offs of Debts by DFSC (FY 1988 and FY 1989)

APPENDIX D - Summary of Supporting Documentation at DFSC
Headquarters or Defense Fuel Regions for
Bulk Fuel Deliveries

APPENDIX E - Summary of Potential Monetary and Other Benefits
Resulting from Audit

APPENDIX F - Activities Visited or Contacted

APPENDIX G - Report Distribution

APPENDIX A. SAMPLING PROCEDURE

We identified a universe of 8,299 payment vouchers that DFSC paid during FY's 1988 and 1989. These payment vouchers had a total value of \$6.6 billion. Our sampling objective was to select a sample of payment vouchers with adequate coverage for the entire universe.

The sample was stratified into three categories, showing the number of payment vouchers and dollar range, as follows:

	<u>Dollar Range</u>	<u>Number of Payment Vouchers</u>	<u>Value of Payment Vouchers (Millions)</u>	<u>Sample Size</u>
Stratum 1	Less than 100,000	4,154	\$ 132.9	60
Stratum 2	100,000 to 1,000,000	2,386	1,200.0	125
Stratum 3	Greater than 1,000,000	<u>1,759</u>	<u>5,300.0</u>	<u>190</u>
Total		<u>8,299</u>	<u>\$6,632.9</u>	<u>375</u>

Our randomly selected sample of 375 payment vouchers was valued at \$629.6 million. The results from the review of the 375 sample payment vouchers and projected results are shown below. The confidence level was 95 percent with a margin for error of ± 10 percent of the estimated dollar amount.

SAMPLE RESULTS

<u>Stratum Dollar Range</u>	<u>Sample Vouchers</u>	<u>Sample Value (Millions)</u>	<u>Total Overpayments</u>	<u>Overpayments Not Collected Within 30 Days</u>	<u>Uncollected Interest</u>
Less than 100,000	60	\$ 1.8	\$ 34,159	\$ 23,268	\$ 383
100,000 to 1,000,000	125	64.6	661,718	337,071	5,448
Greater than 1,000,000	<u>190</u>	<u>563.2</u>	<u>8,167,279</u>	<u>3,600,856</u>	<u>61,198</u>
Total	<u>375</u>	<u>\$629.6</u>	<u>\$8,863,156</u>	<u>\$3,961,195</u>	<u>\$67,029</u>

APPENDIX A. SAMPLING PROCEDURE (cont'd)

PROJECTED RESULTS

<u>Stratum</u> <u>Dollar Range</u>	<u>Total</u> <u>Overpayments</u> (<u>Millions</u>)	<u>Total</u> <u>Vouchers With</u> <u>Overpayments</u>	<u>Overpayments</u> <u>Not Collected</u> <u>Within 30 Days</u> (<u>Millions</u>)	<u>Vouchers With</u> <u>Overpayments</u> <u>Not Collected</u> <u>Within 30 Days</u>	<u>Interest Cost</u>
Less than 100,000	\$ 2.5	1,246	\$ 1.7	552	\$ 28,278
100,000 to 1,000,000	12.3	1,069	6.2	496	104,544
Greater than 1,000,000	<u>76.9</u>	<u>880</u>	<u>33.9</u>	<u>445</u>	<u>574,308</u>
Total	<u>\$91.7</u>	<u>3,195</u>	<u>\$41.8</u>	<u>1,493</u>	<u>\$707,130</u>

APPENDIX B. SAMPLE OVERPAYMENTS WITH INTEREST LOST (FY 1988 AND FY 1989)

<u>Voucher Number</u>	<u>Contract Number</u>	<u>Overpayment</u>	<u>Interest Lost</u> ^{1/}	<u>Days Outstanding</u> ^{2/}
0000390013	87D0495	\$ 1,247	\$ 10	32
0000270004	86D0857	245	4	61
0001310013	87D0606	636	8	45
0002300015	87D0474	14,518	282	80
208678	88D0473	736	6	31
2429	88D0609	2,864	42	55
2001000003	88D0606	1,685	15	31
0001710020	88D0608	1,337	16	47
0000110002	86D0626	7,447	192	101
0000110018	87D0518	11,624	112	38
0000160013	87D0482	11,661	172	58
0000400009	87D0609	23,858	257	42
2000760003	87D1379	31,553	970	120
0001190020	87D0576	2,262	66	114
0001160009	87D0551	20,873	241	45
0001260010	87D0518	3,872	58	59
0001760016	88D0520	9,219	93	40
0001770014	88D0520	18,800	191	40
0001940003	97D0565	3,663	53	57
0001950008	87D0599	10,964	384	124
0001990013	88D0476	23,607	299	50
0002040022	88D0493	28,561	326	45
2002210002	87D0564	22,553	259	45
0000110003	87D0568	4,234	61	54
0000180009	88D0457	13,824	653	245
2000070002	87D0555	651	6	35
0000450016	88D0570	4,621	32	45
0000060017	88D0523	19,703	200	38
0001020006	88D0520	16,357	135	31
0001100009	88D0555	10,943	192	67
0001810034	89D0489	12,393	127	41
2001600001	88D0606	5,062	3	40
0002000015	88D0592	4,982	39	31
0002090004	88D0570	13,784	327	96
0000010024	87D0636	22,821	470	82
0000160017	87D0507	344,779	3,278	38
2002310005	87D0489	26,609	214	33
0000140008	87D0482	19,851	599	118
0000450008	87D0485	72,720	598	59
2000240002	87D0489	26,144	241	36
0000710001	83D0542	31,489	363	45
0000210009	87D0634	51,067	748	59
0000980005	87D0507	273,058	11,687	167
0001150001	87D0469	77,122	1,918	97
2001270001	87D0489	120,404	1,800	59
200002000	87D0527	78,752	902	50

APPENDIX B. SAMPLE OVERPAYMENTS WITH INTEREST LOST (FY 1988 AND FY 1989) (cont'd)

<u>Voucher Number</u>	<u>Contract Number</u>	<u>Overpayment</u>	<u>Interest Lost</u>	<u>1/</u>	<u>Days Outstanding</u>	<u>2/</u>
0001630011	88D0484	\$ 4,383	\$ 62		57	
0001730015	88D0460	49,551	741		59	
0001850013	88D0517	31,592	328		41	
0001920026	88D0526	52,428	758		57	
2001710005	88D0498	58,440	689		60	
0002230020	88D0521	244,948	2,502		42	
0002290004	87D0590	15,694	175		44	
0002350009	87D0590	58,751	655		44	
0002360005	87D0590	78,571	876		44	
0002360013	88D0476	98,814	1,787		69	
0002390019	88D0476	99,259	1,795		69	
0000030007	88D0476	96,064	2,073		82	
0000120001	87D0566	88,016	1,105		47	
0000130002	87D0550	68,763	1,947		106	
0000190009	88D0495	142,967	1,370		36	
0002280002	87D0566	131,594	1,652		47	
0002310007	87D0566	39,340	494		47	
0000030009	88D0508	48,634	700		54	
0000050022	88D0514	688	8		46	
0000510004	88D0514	21,667	220		38	
0002120011	88D0514	76,078	752		39	
2000020004	88D0498	46,732	435		35	
0000340014	88D0516	21,886	257		44	
0000660005	88D0526	26,676	456		64	
2000640002	88D0488	80,749	1,510		70	
0001330003	88D0508	20,294	248		48	
0001610002	88D0514	147,765	2,032		55	
0001710034	89D0530	208,987	2,456		47	
0001890025	89D0463	25,996	247		38	
0001920003	89D0528	90,351	1,531		44	
0001990019	89D0528	39,865	788		79	
0002000022	89D0480	5,673	70		49	
0002050024	89D0482	15,580	210		54	
0002100030	89D0539	141,776	5,729		166	
0002230002	88D0552	56,247	1,456		102	
0002310013	89D0470	21,220	266		50	
		\$3,961,194	\$67,029			

1/ Interest amount that should have been collected when payment or an offset was made. However, since the contractors were not billed for the overpayment by DFSC, the contractors were under no legal obligation to pay interest.

2/ Days outstanding were determined from the date of the final price modification and the date that an offset was made on a subsequent payment to the contractor.

APPENDIX C. WRITE-OFFS OF DEBTS BY DFSC (FY 1988 AND FY 1989)

<u>Contract Number</u>	<u>Date Written Off</u>	<u>Amount Written Off</u>
81D0473	September 1988	\$ 69,221
81D0394	May 1989	188,360
83D0469	May 1989	28,773
83D0469	May 1989	37,086
81D0386	September 1989	114,793
81D0386	October 1989	114,505
		<u>\$552,738</u>

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**APPENDIX D. SUMMARY OF SUPPORTING DOCUMENTATION AT DFSC HEADQUARTERS
OR DEFENSE FUEL REGIONS FOR BULK FUEL DELIVERIES**

<u>Fuel Delivery Location</u>	<u>Total Fuel Deliveries</u> <u>Reviewed 1/ at DFSC</u>	<u>Total Reports 2/</u> <u>Not Available</u>	<u>Total Reports 2/</u> <u>Without Certification Signature</u>
DFR - Central	183	0	65
DFR - Northeast	25	0	0
DFR - Pacific	44	6	5
DFR - South	280	1	0
DFR - West	<u>91</u>	<u>3</u>	<u>0</u>
Totals	<u>623</u>	<u>10</u>	<u>70</u>

1/ Defense Fuel Supply Center Headquarters

2/ Material Inspection and Receiving Reports (DD Form 250/250-1) were either not available or not certified at Defense Fuel Supply Center Headquarters and the appropriate Defense Fuel Region.

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**APPENDIX E. SUMMARY OF POTENTIAL MONETARY AND OTHER
BENEFITS RESULTING FROM AUDIT**

<u>Recommendation Reference</u>	<u>Description of Benefits</u>	<u>Amount and/or Type of Benefit</u>
A.1.	<u>Compliance</u> - Establish negative accounts payable as accounts receivable in accordance with DoD Manual 7220.9-M and send out billings to contractors if immediate offsets cannot be made.	<u>Nondeterminable.</u> By promptly billing and collecting overpayments to contractors, DFSC would improve the liquidity of the Defense Stock Fund.
A.2.	<u>Economy and Efficiency</u> - Implement the procedures necessary to comply with the Debt Collection Act of 1982 (Public Law 97-365).	<u>Funds Put to Better Use.</u> The U.S. Treasury will avoid \$2.1 million in interest costs either through DFSC promptly billing and collecting debts owed by contractors or through interest income paid to the U.S. Treasury on delinquent contractor payments. This will decrease the amount of borrowing needed by the U.S. Treasury.
B.1.	<u>Compliance</u> - Establish controls to ensure that write-off procedures are in compliance with DLA Manual 7000.1.	<u>Nondeterminable.</u> We were unable to quantify the amount of funds that would not be improperly written off due to improved internal controls.

**APPENDIX E. SUMMARY OF POTENTIAL MONETARY AND OTHER
BENEFITS RESULTING FROM AUDIT (cont'd)**

<u>Recommendation Reference</u>	<u>Description of Benefits</u>	<u>Amount and/or Type of Benefit</u>
B.2.	<u>Internal Control -</u> Initiate collection of debts improperly written off.	<u>Funds Put to Better Use.</u> Collection of up to \$552,738 of contractor debts.
C.	<u>Internal Control -</u> Establish policy that requires review of certifications on material inspection and receiving report prior to payment to contractors.	<u>Nondeterminable.</u> We were unable to determine if payments were made for fuel not delivered. Implementation of the recommendation will provide necessary assurance that fuel was actually delivered.

APPENDIX F. ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Assistant Secretary of Defense (Production and Logistics),
Washington, DC
Comptroller of the Department of Defense, Washington, DC

Defense Logistics Agency

Office of the Comptroller, Alexandria, VA

Defense Fuel Supply Center

Headquarters, Defense Fuel Supply Center, Alexandria, VA
Defense Fuel Region - Central, St. Louis, MO
Defense Fuel Region - Northeast, McGuire Air Force Base, NJ
Defense Fuel Region - Pacific, Honolulu, HI
Defense Fuel Region - South, Houston, TX
Defense Fuel Region - West, San Pedro, CA

Department of the Air Force

Bergstrom Air Force Base, Austin, TX
Hickam Air Force Base, Honolulu, HI

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APPENDIX G. REPORT DISTRIBUTION

Office of the Secretary of Defense

Comptroller of the Department of Defense
Assistant Secretary of Defense (Production and Logistics)
Assistant Secretary of Defense (Public Affairs)

Department of the Navy

Naval Audit Service

Department of the Air Force

Air Force Audit Agency

Defense Agencies

Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Commander, Defense Fuel Supply Center
Defense Logistics Studies Information Exchange

Non-DoD Federal Organizations

Office of Management and Budget
U.S. General Accounting Office, NSIAD Technical Information Center

Congressional Committees:

Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
Senate Ranking Minority Member, Committee on Armed Services
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Ranking Minority Member, Committee on Appropriations
House Committee on Armed Services
House Committee on Governmental Operations
House Subcommittee on Legislation and National Security,
Committee on Government Operations

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PART IV - MANAGEMENT COMMENTS

Defense Logistics Agency

COMMENTS OF THE DEFENSE LOGISTICS AGENCY



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



IN REPLY
REFERRED TO DLA-CI

10 MAY 1991

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Report on the Audit of Controls Over Fuel Payments
(Project No. OLC-0026)

This is in response to your 07 March 91 memorandum requesting our
comments pertaining to the audit of Controls Over Fuel Payments
(Project No. OLC-0026). The attached positions have been approved.

5 Enc.

R. Connell
RICHARD J. CONNELLY
Comptroller
Defense Logistics Agency

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0026)

FINDING A: DFSC was not complying with the provisions of DoD Accounting Manual 7720.9-M or Public Law 97-385, 'Debt Collection Act,' or the intent of GAO's recommendation to properly record and promptly collect overpayments made to contractors on bulk fuel purchases. Overpayments made to contractors were classified as negative accounts payable instead of accounts receivable in the accounting records, and DFSC rarely submitted billings to contractors for overpayments. Collections were accomplished by offsetting negative accounts payable balances against later invoices submitted by contractors. When offsets were not made within 30 days, no interest could be assessed against the contractors, as prescribed by the Debt Collection Act, because DFSC had not billed the contractors for the debts. In FY's 1988 and 1989, we estimate that the U.S. Government incurred about \$707,130 in unnecessary interest cost because DFSC allowed contractors to retain overpayments of about \$41.8 million longer than 30 days. If the current accounting and collection practices continue and the same pattern of interest rates and fuel price fluctuations occur, we estimate that the U.S. Government could incur unnecessary interest cost of about \$2.1 million over the 6-year Future Years Defense Program.

DLA COMMENTS: Concur. DFSC inherited the above condition from Defense Logistics Agency Administrative Support Center and was cited in previous GAO review. At the time of the subject audit, corrective measures were in process and near full implementation. To date, corrective measures have been fully implemented as follows:

1. Accounts payable balances are reviewed daily for accuracy and specifically to identify negative entries.
2. Negative entries to Accounts Payable balances are researched to determine the cause. Using a 'worst case' scenario, it takes 30 days to adequately research a negative entry to Accounts Payable. If the negative entry is the result of an overpayment the amount is recorded as an Accounts Receivable.
3. In compliance with the DoD Accounting Manual (DoDM 7220.9-M) and the Debt Collection Act, the 'overpayment' is remedied by offsetting the amount owed against a vendor's subsequent invoice. If a subsequent invoice is not 'in house' when the overpayment is discovered, a demand letter is sent to the vendor without delay. If the payment is not received in accordance with the demand letter, interest is assessed.

The savings reported by the auditors may have been reasonable for the period of their review. However, the projected savings would not be appropriate because corrective actions taken by DFSC would negate any further savings. Therefore, the estimate of \$707,130 in FY's 1988 and 1989 would not be a viable projection for future savings because accounting and collection practices are different than those that were used in the review period of the audit.

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 81

DLA APPROVAL: Richard J. Connolly, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0028)

RECOMMENDATION A.1: We recommend that the Commander, Defense Fuel Supply Center, promptly record all overpayments made to contractors as accounts receivable in official accounting records to comply with provisions of DoD Accounting Manual 7220.9-M and bill contractors for overpayments when immediate offsets cannot be made.

DLA COMMENTS: Concur. Accounting and collection practices have improved significantly since the period reviewed by the auditors. In compliance with the DoD Accounting 7220.9-M and the Debt Collection Act, the DFSC bills contractors in a reasonable period of time when offsets cannot be made against contractor payments. Accordingly, because of the actions and procedures that are currently used at DFSC no further action is necessary at this time.

DISPOSITION:

Action is ongoing; Final Estimated Completion Date:
 Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
 Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
 Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connally, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No: OLC-0026)

RECOMMENDATION A.2: We recommend that the Commander, Defense Fuel Supply Center, assess interest on overpayments retained by contractors in excess of 30 days after being billed to comply with provisions of the Debt Collection Act.

DLA COMMENTS: Concur. DFSC current collection practices use demand letters to contractors that contain the statement. interest will be assessed on unpaid balances not received in 30 days. The current DFSC procedures appear adequate to ensure interest on unpaid balances is assessed on balances in excess of 30 days after being billed.

DISPOSITION:

() Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

-) Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- X) Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
-) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connelly, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0026)

FINDING B: DFSC was not complying with the provisions of DLAM 7000.1, 'Accounting and Finance Manual,' for writing off debts that contractors owed to DFSC. This occurred because DFSC's Accounting and Finance Office removed negative accounts payable balances (amounts owed to DFSC by contractors) from its financial records without attempting to recover these funds. The removal of negative accounts payable balances above \$600 represented a write-off of debt, which DFSC was not authorized to do without approval from higher authority. As a result, DFSC did not recover \$553,000 from contractors, which reduced the financial resources of the Defense Stock Fund.

DLA COMMENTS: Concur. DFSC has performed additional research and some amounts were found to be improperly written off. The improperly written off amounts were inherited from the Defense Logistics Agency Administrative Support Center and were written off for lack of documentation that would have supported a claim. The improperly written off amounts have been reestablished as claims and subject to collection.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

-) Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- X) Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
-) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connelly

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0026)

RECOMMENDATION B.1: We recommend that the Commander, Defense Fuel Supply Center, establish controls to ensure that write-off procedures are in compliance with Defense Logistics Agency Manual 7000.1, that demand letters be sent to contractors for debts owed to DFSC, and that if debts are not promptly collected, forward them to Headquarters, Defense Logistics Agency, for collection.

DLA COMMENTS: Concur. Corrective measures have been implemented, to ensure compliance with Defense Logistics Agency Manual 7000.1, therefore, no further action is required.

DISPOSITION:

() Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance

ACTION OFFICER: Stephen J. Zavada, Jr. DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller. 8 May 91

DLA APPROVAL: Richard J. Connelly, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0028)

RECOMMENDATION B.2: We recommend that the Commander, Defense Fuel Supply Center, establish claims receivable accounts for the six debts owed by contractors totaling \$552,738, submit demand letters for these debts, and if not promptly collected, refer the debts to Headquarters, Defense Logistics Agency for further collection actions.

DLA COMMENTS: Concur. Corrective measures have been implemented to establish claims receivables as recommended. The claims will be processed for collection in accordance with DLA Manual 7000.1, however, as opposed to Headquarters, Defense Logistics Agency, uncollected debts are referred to the Defense Finance and Accounting Service.

DISPOSITION:

(X) Action is ongoing; Final Estimated Completion Date: September 91.

() Action is considered complete.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- () Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- (X) Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connolly, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0028)

FINDING C: DFSC paid contractors for fuel without adequate evidence that the fuel was delivered. This occurred because DFSC did not ensure that receipt documents for bulk fuel deliveries were obtained or included proper certification by a Government representative before making payments to contractors. As a result, when we reviewed supporting documentation for 623 fuel deliveries, we found that DFSC did not have any documentation at the Defense Fuel Regions (DFR's) to support 15 (2 percent) of the deliveries. For another 151 (24 percent) of the deliveries, the DFR's did not have the appropriate certification signature of a Government representative on the receipt documents.

DLA COMMENTS: Nonconcur. The focus of Finding C is on the DFSC Defense Fuel Regions (DFRs) where the DoDIG made an attempt to perform a physical verification of certified (signed DD-250s/250.1) bulk fuel receipt documents. The DoDIG visited five DFR's and found that DFR Central had the largest percentage of uncertified receipt documents. However, DFSC has noted that a major percentage of DFR Central's fuel deliveries are relative to destination contracts. For destination contracts, the fuel is transported directly from the supplier to the customer. The destination shipment and payment process is summarized as follows:

- o The customer/receiver has access to Defense Fuels Automated Management System (DFAMS).
- o The customer/receiver inputs data indicating receipt.
- o The customer/receiver physically retains the receipt document.
- o From data entered by the customer/receiver, DFAMS generates a report indicating shipment and receipt. The DFAMS report is generated at HQ DFSC.
- o The supplier submits an invoice to HQ DFSC and DFSC payment personnel match the invoice to the DFAMS report, pays the supplier and requests reimbursement from the customer/receiver.

DFAMS is a required and certified automated integrated accounting, supply and inventory system and should be relied upon until such time that test performed prove contrary. The DoDIG did not find an internal control weakness, for example an erroneous or fraudulent payment to a contractor. Accordingly, it is our opinion that this finding be deleted from the final audit report.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

- Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: B.N. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connelly, Comptroller

COMMENTS OF THE DEFENSE LOGISTICS AGENCY (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 10 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Report on the Audit of Controls Over Fuel Payments (Project No. OLC-0026)

RECOMMENDATION C: We recommend that the Commander, Defense Fuel Supply Center, issue policy to require that Defense Fuel Regions ensure that they have accurate, complete, and properly certified material inspection and receiving reports (DD 250/250.1) before fuel delivery information is entered into the Defense Fuels Automated Management System.

DLA COMMENTS: Nonconcur. The DoDIG recommendation would require the customer/receiver to forward a copy of the receipt document to either the DFR or HQ DFSC and DFSC would pay the supplier only upon receipt of a certified/signed DD 250/250.1. This procedure would generate additional paper work, duplicate the DFAMS process and slow the payment process. The DoDIG recommended procedure does not strengthen internal controls. The DoDIG methodology is contrary to total quality management. It is our recommendation that this recommendation be deleted from the final audit report.

DISPOSITION:

() Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

(X) Nonconcur. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
() Concur; however, weakness is not considered material. (Rationale must be reflected in the DLA Comments and documentation must be maintained with your copy of the response.)
() Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Stephen J. Zavada, Jr., DLA-CFS

REVIEW/APPROVAL: R.M. Crossley, Acting Chief Accounting and Finance Division, Office of Comptroller, 8 May 91

DLA APPROVAL: Richard J. Connelly, Comptroller

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